



COMMITTEE ON BUDGET & FISCAL REVIEW  
Room 5019, State Capitol  
Sacramento, CA 95814

SENATOR MARK LENO, CHAIR

**MAJOR ACTION REPORT**

June 15, 2011

The purpose of this Major Action Report is to provide a review of the package of budget solutions proposed for adoption June 15, 2011 to balance the 2011-12 budget.

If you have additional questions, please contact the Committee at (916) 651-4103.

## 2011-12 Budget Package

### **Legislature Moves Balanced Budget Forward**

On May 16, the Governor released his May Revision for budget year 2011-12. The Governor indicates the remaining and adjusted General Fund (GF) deficit is \$10.8 billion for the two-year period ending June 30, 2012. This includes a \$1.2 billion reserve.

In January, the estimated GF shortfall was \$27.6 billion – including a \$1.0 billion reserve and including the cancelation of the sales-leaseback transaction. In March, the Legislature passed \$14 billion in solutions, primarily spending reductions.

The Senate adopted most of the Governor’s May Revision framework that relied on approximately \$11 billion in additional revenues. However, after failing to gain the Republican votes needed to move forward the revenue portions of the Governor’s framework, the Senate has identified alternative solutions to ensure a balanced budget.

The Senate adopted the vast majority of the Governor’s proposed expenditure reductions. However, the joint legislative version of the budget does restore approximately \$200 million in child care cuts within Proposition 98 and approximately \$140 million in CalWORKs reductions that were made in the March package.

In addition to the reductions already adopted, the joint legislative version incorporates the following major changes to balance the budget for 2011-12 without two-thirds revenues. This includes \$10.4 billion in additional solutions, which will result in a slightly lower budgetary reserve of approximately \$575 million General Fund in the budget year. The major amendments to the Governor’s proposal to replace revenues include the following.

#### **Adopt additional expenditure reductions:**

- Reduces K-14 Proposition 98 funding by approximately \$3 billion compared to the Governor’s May version by continuing deferrals of \$3 billion. The final version also eliminates the additional \$744 million in settle up payments assumed in the June 8 Senate version.

- Assumes \$1 billion from savings in children’s Medi-Cal services from reducing and redirecting \$1 billion in local Proposition 10 funding. This assumption returns to the proposal adopted in the March 2011 budget package and assumes the State prevails in the current litigation.
- Includes an additional \$150 million reduction to the University of California system that could be restored if additional General Fund revenues are received. This reduction is in addition to the \$500 million reduction included in the budget package passed in March. Also assumes a new cash solution by deferring the June payment to the UC system until after the end of the fiscal year in August 2012.
- Includes an additional \$150 million reduction to the California State University (CSU) system that could be restored if additional General Fund revenues are received.
- Includes an additional \$150 million reduction to the trial court system that could be restored if additional General Fund revenues are received.
- Adopts \$50 million in General Fund savings from dedicating surplus county office of education property tax balances that are currently restricted to other education programs, thereby reducing State General Fund costs.

**Adopt majority vote revenues:**

- Assumes \$1.2 billion from the assumption of a revised state building lease transaction.
- Ends the “revenue exchange period” that was enacted in 2004. This action increases local sales and use tax by ¼ percent, which results in a commensurate transfer of property tax from local government to schools in order to save approximately \$900 million General Fund.
- Increases vehicle registration fees by approximately \$12 to defray the costs associated with the Department of Motor Vehicles. This action frees up \$300 million in vehicle license fees to be dedicated to local governments that can be used as a down payment for the implementation of public safety realignment. Additional actions will need to be taken in the coming weeks to ensure that public safety realignment is funded appropriately; including addressing the \$504 million in funding historically dedicated to local public safety programs.

- Adopt a State Responsibility Area Fee to cover some costs of state fire suppression on privately-owned lands. Reduce General Fund support for Cal-Fire by \$150 million and replace with fee revenue. Also shift additional General Fund costs related to timber harvest plans to fees.

**Updated revenue assumptions:**

- Assumes current revenue trends continue and generate approximately \$815 million General Fund above the revenue estimates in the Governor's May Revision. This is consistent with the most recent data on revenues collected by the State since the Governor's May Revision was released.

**Other Solutions:**

- Assumes \$700 million in additional one-time federal funds to offset General Fund costs related to the Medi-Cal program.

## Major Expenditure Reductions

Overall, the Senate version of the budget prioritizes K-12 education. Significant reductions were made in the Health and Human Services areas, but in many cases, alternative cuts were found that mitigate the harshest of these reductions. Most areas of the budget saw significant expenditure reductions.

**K-12 Education.** The Senate version of the budget includes funding for Proposition 98 that is about the same level as the current fiscal year. This is approximately \$3 billion less than the level proposed in the Governor's 2011 May Revision. The lower spending on Proposition 98 is a result of not including the Governor's proposed two-thirds vote taxes in the final budget package. Overall Proposition 98 expenditure will be approximately \$49.7 billion in the budget year. Major proposals included in the Senate package include the following:

- **Deferrals:** Continues approximately \$3 billion in inter-year K-12 payment deferrals, consistent with the Governor's January proposal.
- **Student Mental Health Services:** Approves Governor's budget proposal to rebench the Proposition 98 guarantee by \$222 million to fund mental health related services for students with disabilities (previously provided by counties per the AB 3632 mandate). Also augmented 2010-11 funding by \$80 million to partially backfill for a funding shortfall created when Governor Schwarzenegger vetoed funding for the AB 3632 mandate.
- **Class Size Reduction:** Approved a one-year extension of the continuous appropriation for the class size reduction categorical program.
- **Categorical Flexibility:** Approved the Governor's proposal to extend various flexibility options to school districts for an additional two years.
- **Secretary of Education Elimination:** Approved the Governor's proposal to eliminate the Office of the Secretary of Education.

**Childcare.** Approved \$300 million in ongoing savings to childcare programs. This is approximately \$200 million less than was previously eliminated in March due to the following actions:

- **Standard Reimbursement Rate Reduction:** Restored 10 percent rate cut to the Title V contracts.
- **Contract Reduction:** Reduced contracts, or slots, including preschool, by 11 percent instead of 15 percent.
- **11 and 12-Year Olds:** Continued funding childcare services for 11 and 12-year olds.
- **Family Fees:** Rejected earlier proposal to increase sharply the family fees paid by low-income individuals for childcare services.

**Higher Education.** Adopted a \$650 million reduction to the University of California, a \$650 million reduction to the California State University, and a \$400 million reduction to the California Community Colleges. Some of these cuts in each segment will be offset with student fees. Also adopted a new inter-year deferral for the University of California of about \$560 million.

**Health and Human Services.** Achieved total expenditure cuts of around \$6.0 billion in the Health and Human Services area, including \$1 billion from using Proposition 10 funds one-time to offset GF costs in Medi-Cal. The Senate version of the budget also adopts the following additional proposals included in the May Revision for an additional \$500 million in savings:

- **Hospital Fee:** Assumes \$320 million in savings from extending the hospital fee for one year as enacted in SB 90 (Steinberg) chaptered in April of this year.
- **Maximizing Federal Funds:** Approved Governor’s proposals to technically modify the use of certified public expenditures to enable California to maximize federal funds and obtain offset of General Fund expenditures.
- **CalWORKS:** Restores approximately \$90 million related to additional grant cuts for safety net and child-only cases that exceed 60 months. Also restores \$50 million of the single allocation, which is the funding used by counties to provide welfare-to-work services.
- **Getting Ready for Health Care Reform:** The Senate version of the budget also approved the Governor’s proposal to transfer administration of Medi-Cal community mental health programs and the Drug Medi-Cal program to the Department of Health Care

Services. This will enable the state to be better positioned for the implementation of health care reform, which will provide greater parity for behavioral health issues.

**Corrections:** Approved expenditure reductions of about \$1.0 billion in Corrections mainly due to the realignment proposal. However, the Senate has also approved the Governor's workforce cap proposal for an additional \$195 million and significant reductions to the Board of Parole Hearings operations. Furthermore, the Senate has restored nearly \$50 million in community-based rehabilitation contracts that will be needed as the State implements realignment.

**Courts:** Approved the Governor's proposal to reduce the courts funding by \$200 million. Also approved an additional \$150 million reduction to the courts that will likely result in court closures. The package also reflects an acknowledgement of an additional \$42 million for workload related to realignment and new workload related to parole revocation activities.

**Transportation:** Approved the Governor's proposal to use truck weight fees to pay about \$1.0 billion in transportation-related general obligation bond debt. Approved re-enactment of the 2010 Tax Fuel Swap to conform to the requirements of Proposition 26.

**Redevelopment:** The Senate's budget package includes a solution from redevelopment agencies (RDAs) that provides a \$1.7 billion General Fund benefit in 2011-12.

**Local Government:** Approved the Governor's proposal to suspend the Williamson Act / Open Space Subvention for a two-year savings of \$20 million.

**Natural Resources and Energy:** Approved a cut of \$155 million in energy efficiency programs funded by the Gas Consumption Surcharge Tax. Approved cuts of \$11 million to State Parks and \$10 million to Off-Highway Vehicle Parks. Also approved \$150 million reduction to Cal-Fire, to be backfilled with new revenues from a State Responsibility Area (SRA) Fee to be paid by homeowners within SRA.

**Government Efficiency and Employee Compensation:** Approved expenditure cuts of about \$700 million in areas such as: employee compensation (\$308 million); employee healthcare (\$80 million); and other state operations-related governmental efficiencies (\$250 million) (discussed further in Page 10 of this document).



## Revenues

**Revenue Package.** The Senate version of the budget does not include the Governor's proposal to maintain 2010 tax rates for five years. This and the Governor's proposal to reform enterprise zones and implement a single sales factor for apportioning corporate income to California would have generated \$11 billion in the current and budget years. This would have resulted in \$1.7 billion in additional expenditures for Proposition 98.

The Senate version does include the following majority vote revenues:

- Assumes \$1.2 billion from the assumption of a revised state building lease transaction.
- Ends the "revenue exchange period" that was enacted in 2004. This action increases local sales and use tax by ¼ percent, which results in a commensurate transfer of property tax from local government to schools in order to save approximately \$900 million General Fund.
- Increases vehicle registration fees by approximately \$12 to defray the costs associated with the Department of Motor Vehicles. This action frees up \$300 million in vehicle license fees to be dedicated to local governments that can be used as a down payment for the implementation of public safety realignment.
- Adopt a State Responsibility Area Fee to cover some costs of state fire suppression on privately-owned lands. Reduce General Fund support for CalFire by \$150 million and replace with fee revenue. Also shift additional General Fund costs related to timber harvest plans to fees.

## **PUBLIC SAFETY REALIGNMENT**

Originally, the Senate version of the budget package contained the Governor's revised public safety realignment plan. However, with no new revenues and no constitutional amendment, this plan has become more difficult to implement and is, therefore, largely not a part of the Senate version. However, the Legislature passed AB 109 in March that realigned low-level offenders from state prison to local jurisdiction. This policy change does not go into effect until funding is provided to support this realignment of offenders. The Senate continues to pursue implementation and funding for AB 109.

The realignment plan continues to be essential especially in light of the recent U.S. Supreme Court decision that affirmed the lower court's decision to require the reduction of overcrowding in the state prison system. The State has two years to reduce the prison population by over 30,000 inmates. Realignment will allow the state to accomplish this reduction in a way that has significant potential benefits for public safety. Funded realignment will allow for funding to flow with the offender back to the community where it can be invested in support services, programs, and law enforcement that enhance the safety of communities.

The Senate version includes \$300 million in vehicle license fee revenues freed up from increasing the registration fees to cover costs at the Department of Motor Vehicles. Additional actions will need to be taken in the coming weeks to ensure that public safety realignment is funded appropriately; including addressing the \$504 million in funding historically dedicated to local public safety programs.

## **REDUCING STATE GOVERNMENT**

### **Senate Streamlines Government and Eliminates 20 Boards & Commissions**

The Senate version of the budget package eliminates 20 boards and commissions that were proposed for elimination in the Governor's May Revision. The Senate also adopted policy to put in motion a major reorganization and consolidation of various health care programs that when fully implemented may result in the further elimination of additional agencies. These actions will help the Governor achieve the \$250 million GF savings identified in March 2011 related to efficiencies in state government operations. The mechanism to achieve these savings is a budget control section that provides the Administration with the authority to make the required budgetary reductions to achieve the total savings.

The Administration has identified, and in some cases already achieved, savings through a variety of executive actions, including eliminating the offices of the Secretary of Education and the American Recovery and Reinvestment Act Inspector General, banning non-essential travel, implementing a statewide building rental rate reduction, reducing the number of state-issued cellular phones, and reducing the statewide vehicle fleet, including the elimination of any non-essential vehicles and reducing the number of home-storage permits.